

IEEC Cross #

Exhibit No. 3

ICC Docket No. 05-0159

Witness

Commonwealth Edison Company's Response to

IEEC Data Requests 1.01 Through 1.48

Dated: April 8, 2005

Reporter

9-9-05

HLB

**REQUEST NO. IIEC 1.07:**

Referring to ComEd Exhibit 3.0, please explain why and how ComEd determined that a 50% load cap for the CPP and CPPH auctions was appropriate?

**RESPONSE:**

Please refer to the testimony, Exhibit 3.0 lines 1024 through 1033 and to Exhibit 4.0 lines 1462 through 1531 for a discussion on load caps. ComEd received feedback from various stakeholders. Suppliers that had participated in the New Jersey auctions were typically in favor of load caps at lower levels, supporting the view that lower load caps could promote bidder participation. Customer groups were typically in favor of higher load caps citing their concerns that load caps might limit low cost suppliers and have a negative price impact.

In deciding on an appropriate value for the load cap, ComEd took into consideration this feedback and further considered the primary purposes of establishing load caps, namely:

- to encourage broader participation of suppliers
- to diversify credit risk over a larger group of winners
- to limit the ability of suppliers to withdraw profitably
- to limit the ability of suppliers to over-represent their initial interest in the auction.

While there are trade-offs on setting any value for the load cap, ComEd felt that the 50% level strikes a reasonable balance and satisfies the purposes mentioned above. ComEd presented these observations to Dr. LaCasse. ComEd asked her to evaluate a 50% load cap proposal. Dr. LaCasse provided advice regarding the role of load caps in the mechanics of the auction process to ComEd. Dr. LaCasse provided her opinion on the proposal as detailed in her testimony, based on the role of load caps, her experience as Auction Manager in the New Jersey Auction, and based on the number of tranches won by suppliers historically as detailed in Exhibit 4.6.

**ICC Docket No. 05-0159**

**Commonwealth Edison Company's Response to  
IIEC Data Requests 6.01 Through 6.13  
Dated: July 14, 2005**

**REQUEST NO. IIEC 6.05:**

Please refer to the Rebuttal Testimony of Dr. LaCasse (ComEd Exhibit 11.0) at 24- 28. In her evaluation of the load caps, has Dr. LaCasse performed any simulations of the proposed ComEd auction using any examples of likely bidding patterns considering the combination of bidder uncertainty, strategic bidding, and information supplied to bidders? If yes, please provide all output or reports of such simulations and any software or other tools used in conducting them. Did Dr. LaCasse perform any simulation of auction-clearing prices specifically using a load cap of 33%? 50%? 100%? If yes, please provide the results of such simulations. How do the results of these simulations compare?

**RESPONSE:**

No, Dr. LaCasse has not performed any simulations.

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**REQUEST NO. IIEC 6.06:**

Please refer to the Rebuttal Testimony of Dr. LaCasse (ComEd Exhibit 11.0) at 26- 29. Dr. LaCasse describes the following factors in evaluating load caps:

- a. Limiting participation,
- b. Influence on auction results,
- c. Over-stating interest, and
- d. Diversification.

In Dr. Lacasse's opinion, which one of these factors will have the largest impact on the auction-clearing prices? How does the magnitude impact of this factor compare to the magnitude impacts of the other three factors? Has Dr. LaCasse performed any simulations of the proposed auction specifically evaluating these factors and their impacts on auction-clearing prices? If yes, please provide all output or reports of such simulations and any software or other tools used in conducting them.

**RESPONSE:**

Dr. LaCasse does not believe that it is possible to predict which of factors a, b or c will have the "largest impact on the auction-clearing prices." Dr. LaCasse does not believe that simulations would be helpful in this regard. As noted in the response to Date Request IIEC 6.05, Dr. LaCasse has not performed any simulations.

Dr. LaCasse notes that with respect to factor d, diversification, the objective of diversification is to limit the utility's and the customers' exposure to the default of a single supplier. Hence, in this case, the auction-clearing price may be less relevant than the total costs of serving customers. The total costs could include higher replacement costs associated with the default of a supplier that would not be knowable at the time of the auction and would not be reflected in the auction-clearing price.

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**Commonwealth Edison Company's Response to  
HEC Data Requests 6.01 Through 6.13  
Dated: July 14, 2005**

**REQUEST NO. IIEC 6.07:**

Please refer to the Rebuttal Testimony of Dr. LaCasse (ComEd Exhibit 11.0) at 27, lines 658-662. Dr. LaCasse states:

If bidders' indications of early interest, which are made at prices that can be substantially higher than the expected final auction prices, overstate the bidder's willingness to serve, the Auction Manager may conclude that there is more competition at the auction than there truly is.

Please describe how much "substantially higher" prices have to be in order for the Auction Manager to conclude there is more competition than there truly is. What level of magnitude would constitute "substantially higher" prices?

**RESPONSE:**

The quotation from Dr. LaCasse's testimony is taken from her discussion of the factors to consider when setting load caps. The reference to indications of early interest recognizes that the Auction Process provides for bidders to submit indicative offers. The indicative offer specifies two numbers of tranches. The first number is the amount that the bidder is willing to serve at the maximum starting price and the second number represents the amount that the bidder is willing to supply at the minimum starting price. The minimum and maximum starting prices should be set high enough to encourage participation. Competition will tick prices down to their final levels. At the final prices, the supply will have been reduced to be just sufficient to meet the requirements.

Dr. LaCasse takes as a given that a bidder's willingness to supply is higher at higher prices. A bidder's indication of interest at the maximum starting price is expected to be higher than a bidder's willingness to supply at the final auction price. The minimum and maximum starting prices will be substantially higher than the expected final auction prices, regardless of the level of the load cap. The potential overstatement of the "bidder's willingness to serve" is related to the level of the load cap. The load cap – not the extent to which minimum and maximum starting prices exceed the expected final auction prices – determines the amount by which a bidder can overstate its early interest in the auction. As Dr. LaCasse stated in her rebuttal testimony, "[t]he higher the load cap is compared to the typical bidder's appetite for the product

on offer, the greater is the scope for a bidder overstating interest early in the auction." (lines 664-666).

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**REQUEST NO. IIEC 6.08:**

Please refer to the Rebuttal Testimony of Dr. LaCasse (ComEd Exhibit 11.0) at 27. In the opinion of Dr. LaCasse, would an auction bidder be exposing itself to any financial risk by over-representing its initial interest in the auction? If yes, please explain your answer. Why would Dr. LaCasse expect a bidder to do so?

**RESPONSE:**

Yes, there are potential financial risks or costs to over-representing initial interest in the auction.

With their Part 2 Applications, bidders submit indicative offers. These indicative offers are not binding and therefore there is no financial risk associated with presenting a firm offer. However, bidders must submit letters of credit to support their indicative offers; additional guarantees may also be required. There are costs associated with providing this pre-auction security.

Any bid submitted in the auction is binding and represents a firm offer to supply at the relevant prices for the round. If a bidder over-represented its interest early in the auction, the bidder would be exposing itself to financial risk to the extent that, if the auction ended prematurely, the bidder would win more than it had been ready and willing to serve.

The question implies that since there is a financial risk to over-representing interest in the auction, a bidder would not be expected to do so. Dr. LaCasse disagrees. Drawing conclusions by looking only at the cost is to consider only one side of the equation. Dr. LaCasse believes that whether a bidder could over-represent its early interest at the auction depends on both the costs and the benefits of doing so. The main potential benefit of over-representing interest is explained in the response to IIEC 6.09.

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**REQUEST NO. IIEC 6.09:**

Please refer to the Rebuttal Testimony of Dr. LaCasse (ComEd Exhibit 11.0) at 27. In Dr. LaCasse's opinion, what specific information would a bidder who over-represents its initial interest in the auction have to possess in order to profitably withdraw tranches from the auction?

**RESPONSE:**

As Dr. LaCasse explains in her rebuttal testimony, after round 1 bids are received, the Illinois Auction Rules propose that the Auction Manager would consider whether to cut back the volume to ensure the competitiveness of the auction. The Auction Manager would use a confidential set of guidelines to decide whether to cut back the volume and to determine the magnitude of any necessary cutback. If the volume were cut back, it would be cut back to the number of tranches bid in round 1 divided by a parameter called the target eligibility ratio (a desired ratio of tranches bid to the volume). The target eligibility ratio would be set on the basis of various factors, such as the number of bidders and characteristics of individual bids. The Auction Manager may further revise the volume on the basis of the bids after round 1.

There may be a potential benefit to a bidder that overstates its interest in the auction. If such a bidder maintains interest until volume reduction opportunities have passed, the Auction Manager may set the auction volume based on information that is less reliable than would otherwise have been the case. It is possible that the Auction Manager would believe the competitiveness of the bidding environment sufficient, and would not cut back the volume, while the Auction Manager would have cut back the volume absent the overstatement. If the auction proceeds without a volume cutback when one was in fact necessary to ensure the competitiveness of the bidding environment, then final prices can be expected to be higher than would have been the case if the volume cutback had been initiated.

It is not possible to determine precisely the "specific information" that a bidder would require in order for the potential benefit of over-representing its initial interest to be greater than the potential cost. (Please see the response to Request IIEC 6.08 for a discussion of the cost). It is possible to say that a larger load cap increases the scope for over-representing interest (please see response to Request IIEC 6.07), increasing the potential benefit from over-representing interest. It is also possible to say that if bidders knew the full details of the volume guidelines, bidders could mitigate the risk from over-representing interest. Correspondingly, Dr. LaCasse recommends a load cap that will discipline the ability of bidders to over-represent their interest and Dr. LaCasse also recommends that details of the volume guidelines be kept confidential from bidders.

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**REQUEST NO. IIEC 6.11:**

Please refer to the Rebuttal Testimony of Dr. LaCasse (ComEd Exhibit 11.0) at 30, lines 731-733. Dr. LaCasse states:

Nevertheless, even with this potential cost, I believe that a 33% load cap will be effective and that the cost in terms of limiting participation would still be modest enough to provide a good balance.

Please describe Dr. LaCasse's magnitude of cost that she defines as "modest." Has Dr. LaCasse performed any analysis of the effect of a 33% load cap on the costs associated with limiting the participation of bidders? If yes, please provide all output or reports of such simulations and any software or other tools used in conducting them.

**RESPONSE:**

The use of the word "modest" reflects Dr. LaCasse's qualitative assessment and expectation. Dr. LaCasse has not performed any simulations and does not believe simulations would provide better guidance than a qualitative assessment.